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Manager of the Year: 1999

by Christine Benz, Eric Jacobson, and Gregg Wolper | One year ago, we began our Manager of the Year essay by noting that 1998 had been "a trying year for most mutual-fund managers." For domestic stock-pickers, the S&P 500 index had once again proven to be an embarrassingly elusive target. Meanwhile, international managers had been forced to deal with a collapse in emerging markets--and in many developed ones--after Russia defaulted on its debt.

It was a different story in 1999.

With the explosion in Internet stocks and other technology and telecom shares, many managers not only beat the S&P 500, but they also posted incredibly high returns. The tech frenzy spread around the world, which along with rebounds in Japan and emerging markets helped international funds post healthy, even stunning, gains. Only two types of managers were left out: deep-value devotees and fixed-income managers, who had to battle rising interest rates.

Past Managers of the Year

	Name
1998	Bill Miller, Mark Yockey, Bill Gross, et al.
1997	Mario Gabelli, Helen Young Hayes, David Baldt
1996	Shelby Davis, Hakan Castegren, Joe Deane
1995	Jack Laporte, Jack Mussey, Dan Fuss
1994	Bob Rodriguez
1993	Jeff Vinik
1992	Bill Dutton
1991	Donald Yacktman
1990	Martin Whitman
1989	Tom Marsico
1988	Peter Lynch
1987	Jerry Palmieri

The roster of managers with stellar returns in 1999 is thus a long one. But a strong one-year return isn't the only qualification required to win Manager of the Year. In making our selections, we chose managers who also have demonstrated the investment skill, courage to differ from the consensus, and commitment to shareholders necessary for outstanding long-term performance.

Domestic Stock: Jim Callinan, RS Emerging Growth

In 1999, a year in which nearly 300 funds delivered triple-digit gains, Jim Callinan's fund still stood out.

Indeed, RS Emerging Growth's RSEGX 183% gain for the year was gaudy even for the small-growth category, where returns of 100% or better were commonplace. Chock-full of pricey tech and telecom names, Callinan's charge gained 75% in the fourth quarter alone.

RS Emerging Growth's 1999 return, however, wasn't the only thing that caught our attention. Callinan's fund has been remarkably consistent, even when expensive small-cap stocks haven't had a strong tailwind. For example, in 1997 and 1998, lean years for most small-growth investors, Emerging Growth put up strong absolute numbers.

How has Callinan done it? Good timing explains a lot. In 1997's second half, for example, Callinan backed up the truck for then-unloved Internet stocks, which soon skyrocketed. And this past year, Callinan made a timely shift away from consumer-based Internet plays into business-to-business Net stocks, which dominated the market in 1999's second half.

RS Investment Management also deserves some credit for Callinan's success. RS managers have long been allowed a lot of flexibility to make sizable wagers against their benchmarks. Of course, such bets can backfire, but Callinan has been able to avoid big blowups thus far. Callinan's success with an aggressive style comes at the right moment: At a time when mutual funds are increasingly criticized as boring investments for conservative sorts, RS funds have been anything but.

Meanwhile, Callinan's fund has had a central role in a compelling story playing out at RS Investment Management. In late 1998, the firm was reeling from asset outflows and lackluster performance at some of its largest funds. That enabled CEO Randy Hecht and a group of employees to buy the firm from Bank of America for a song--$20 million--just as the stock market was emerging from a funk. The purchase is beginning to look like a steal, as Callinan's hot performance has drawn assets to the family.

Domestic-Stock Runner-Up: Howard Schow, Theo Kolokotrones, and Joel Fried

This team, which runs Vanguard Primecap VPMCX and Vanguard Capital Opportunity VHCOX, has put up hot returns while keeping its feet planted firmly on the ground.

The Dean's List

	1999 Return (%)	1999 Rank	3-Year Rank	5-Year Rank
RS Emerging Growth RSEGX*	182.5	3	1	1*
EuroPacific Growth AEPGX	57.0	23	16	11
Invesco High-Yield FHYPX	9.4	10	7	6

Rank within Morningstar Category. Data as of 12-31-99. *Jim Callinan began managing fund in July 1996.

These valuation-conscious managers scooped up out-of-favor semiconductor names in late 1997, then hung on for spectacular gains at both of their charges in 1998 and 1999. Mid-cap fund Capital Opportunity, a laggard in the Vanguard family before the current team took over, gained nearly 100% in 1999. This team also has a phenomenal long-term record.

International Stock: The EuroPacific Growth Team

It's easy to explain why EuroPacific Growth's AEPGX managers--Stephen Bepler, Thierry Vandeventer, Janet McKinley, Mark Denning, Robert Lovelace, Martial Chaillet, and Alwyn Heong--deserve recognition.

This fund's five-, 10-, and 15-year returns sit near the top of the foreign-stock category, and it has shown remarkable consistency in its year-to-year rankings. In addition, it has provided a smoother ride than practically all its rivals have. This outstanding combination of high returns and low volatility, demonstrated over such a long period, speaks volumes about the managers' skills.

In 1999, the EuroPacific crew took the year's twists and turns in stride and showed how a disciplined, buy-and-hold strategy can flourish even when conditions seem to favor quick trading and risk-taking. Because of their eye for value and their commitment to long-term goals, they had bought many of what turned out to be 1999's best stocks years earlier. For example, they bought current top holding Mannesmann, now a trendy telecom play with spectacular stock-price gains, back when it was a stodgy industrial conglomerate. A glance at the fund's June 1992 portfolio shows Mannesmann as the second-largest position.

Just as important, the managers adjusted to changing market conditions and an exploding asset base. They boosted the fund's Japan holdings significantly in 1999 and sharply increased its technology stake between 1997 and 1999. EuroPacific Growth's assets grew from less than $1 billion at the end of 1990 to roughly $30 billion in 1999. It is by far the biggest foreign-stock fund.

One difference between this group and the typical Manager of the Year winner is, well, the fact that it's a group.

Capital Research & Management divides EuroPacific Growth's assets among a handful of managers who pick stocks separately. They don't worry about index weightings or what rival managers are doing. Also, the fund's managers stick around. Bepler and Vandeventer, for example, have been on the team since the fund's inception in 1984.

The EuroPacific Growth managers follow the tenets that many others just talk about--buy and hold, don't overpay. And they disprove other nuggets of conventional wisdom, such as that huge funds must "revert to the mean" or that emerging markets are too chancy for conservative managers. They set an example that other managers would be wise to follow.

Fixed-Income: Jerry Paul, Invesco High-Yield

In a world where bond-fund management has increasingly become a cookie-cutter, keep-your-head-down business, Invesco's Jerry Paul stands out.

After taking the reins of sluggish Invesco High-Yield FHYPX in mid-1994, Paul turned the fund around. He has amassed a five-year record that places in the upper reaches of the high-yield bond category and blows past the First Boston High Yield index.

Paul's hallmark has been his bottom-up bond-picking skill. An enthusiastic practitioner of fundamental credit research, he has focused on issuers that he thinks are on the verge of a rating upgrade or merger-and-acquisition activity that could improve their creditworthiness. He has excelled in finding bonds whose value was not being recognized by the marketplace

His style does court risk. For example, Paul has owned more than his share of potentially volatile bonds, such as those structured as deferred interest (in essence, zero-coupon) issues and those with lower-tier credit ratings. And at times, the fund has also been highly concentrated in specific sectors--mainly cable, media, and telecom, where merger-and-acquisition activity has been rife. However, Paul knows every issuer and bond structure inside out. That, and his penchant for staying well diversified, has allowed him to almost completely avoid blowups.

Never was his ability more apparent than in 1999. Managers who had let their guard down over the past few years, picking up riskier bonds in search of extra yield, found themselves staring down the barrel of downgrades and defaults, while Paul's portfolio survived unscathed. The fund profited when a host of its bond issuers either went public or benefited from some kind of

merger activity. Names that made headlines in the stock world, such as Qwest Communications and Global Crossing GBLX, produced home runs for Invesco High-Yield, as well.

With the specter of rising interest rates and defaults looming over the bond market, the high-yield sector may not seem the most promising area right now. As long as Paul is at the helm of Invesco High Yield, however, the fund beckons as a top choice for those who want a manager willing to stray from the straight and narrow--and who has enjoyed repeated success by doing so.

Posted 01-06-2000

Christine Benz is domestic-equity-funds editor with Morningstar. Eric Jacobson is Morningstar's bond-funds editor. Gregg Wolper is Morningstar's international-funds editor. Direct questions regarding this article to christine.benz@morningstar.com.

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